

FAQ ISSUE #16 Revised 2/12/12 PASSIVE INCOME VERSUS ACTIVE INCOME

Tax Question:

What is the difference between passive income and active income?

Facts:

Active or business income is income generated from a profession, calling, trade, manufacture, adventure or concern in the nature of trade. In other words income that is generated from an activity.



Passive or property income is a return on invested capital such as rent, interest, dividends and royalties. Little or no effort is required to produce the return.

Discussion:

Income is taxed in companies at different rates depending on the type of income. In a BC resident Canadian Controlled Private Company (CCPC) the first \$500,000 of active income is taxed at the low rate of tax of 13.5%. Passive income does not benefit from this low rate. Irrespective of how much profit a CCPC makes, passive income is taxed at the high rate of corporation tax plus an additional 6-2/3% of refundable tax.

The political reason behind this two tiered approach is that active income contributes more to the economy through employment, goods and services, innovation and infrastructure than passive income. Therefore, the tax system is designed to encourage the generation of active income rather than the pursuit of passive income.

Recommendation:

If you are unsure about the type of income your business generates, please contact Gilmour Knotts Chartered Accountants .

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